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Tax News

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TAX NEWS

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The 1949 Revenue Act

Leaders in the 81st Congress have announced that they are in no hurry to take up proposed changes in the tax laws, preferring to wait until nearer the close of the current fiscal year that the country's financial situation may be reviewed. In the meantime, individual members have introduced at least six bills in the House and two in the Senate, ranging from a proposal to reimpose the excess profits tax repealed in 1945 to the recognition, for tax purposes, of family partnerships based on a gift. The form of the 1949 Revenue Act is still too indefinite to encourage speculation, but the experts seem sure that the small corporation is most likely to retain present advantages in any event.

Capital Gains of Radio Stars

Not that we have any inside information on the Amos 'n Andy ruling by the Bureau of Internal Revenue, nor on the Treasury's refusal to rule on the Jack Benny Affair, but solely because every tax commentator in America is surmising on these subjects in print, we want those readers who rely on *The Woman C.P.A.* for current tax gossip to hear about it too.

It seems that one day when the highbrows in the Bureau were being more naive than usual, some smart tax practitioner suggested that the Amos 'n Andy radio program about to be sold was just full of capital assets, gain on the sale of which would be taxable at capital gain rates. The s. t. p. obtained a ruling that the sale of the rights to use the name, characters, scripts, plots, slogans, as well as the radio, television, screen, and stage rights of the Amos 'n Andy show would be taxable at capital gain rates.

Probably the Bureau wasn't prepared for the indignant protests of ordinary taxpayers who pay ordinary rates on compensation received in less sizable checks, nor for the demands for investigations by headline-conscious chairmen of Congressional committees. The Bureau hadn't even foreseen the rush of radio stars, headed by Jack Benny, to obtain similar tax-saving rulings. It was too late to recall the Amos 'n Andy ruling but the Bureau did the next most expedient thing—it announced (Press Release S-952, 1-3-49) that "proposals of radio artists and others to obtain compensation for personal services under the guise of sales of property cannot be regarded as coming within the capital gains provisions of the Internal Revenue Code."

Tax gossipers generally seem to believe that Benny may ultimately pay less than ordinary tax rates on at least part of his sale price. He had actually sold his stock in a corporation that produces his radio program. Our own guess is that some internal revenue agent will disallow the capital gain feature of the Amos 'n Andy sale and let the Courts prove again what a slender reed to lean upon is a Bureau ruling. Couzens, 11 BTA 1040.

We are tempted to speculate on the form personal service contracts may take in the future if radio artists' present tax plans should prevail. Edgar Bergen is reported to be planning the sale, at a large increase over the purchase price, of an ingenious hardwood gadget (commonly called charlie mccarthy) used in his trade or business, and then agreeing to display the depreciable asset, for a modest sum, on his knee. We may even expect to hear that burlesque queens are selling unique and highly personalized G-strings for far more than original cost, and then contracting to display and activate the capital asset just sold, accepting a reasonable compensation for "personal services actually rendered" thereafter.

The Interest on Nothing is Nothing

In struggling with the complexities of taxing statutes, regulations, and precedents, both the courts and tax practitioners frequently get so confused that they overlook simple axioms which might point to the solution of the problem. It is refreshing when the courts do hark back to fundamentals, as did Judge Goodrich of the Third Circuit Court of Appeals in the case of Seely Tube and Box Company vs. John E. Manning, as Collector of Internal Revenue for the Fifth District of New Jersey, decided December 20, 1948.

The petitioner was entitled to a refund of 1941 income taxes by reason of a carry-back of 1943 losses. The Commissioner had assessed a deficiency for the year 1941, which had been paid with interest, but the

carry-back wiped out the deficiency and created an overassessment. In keeping with the practice of the Treasury Department, the Commissioner retained, out of the amount to be refunded, the interest on the "potential" deficiency which had existed until offset by the carry-back. The District Court, 76 Fed. Supp. 937, had upheld the Commissioner, but in reversing the District Court, Judge Goodrich decided ". . . that the interest on nothing (what the taxpayer owed) is necessarily nothing."

This CCA-3 decision will bring relief to many taxpayers who have losses carried back to prior years. In our own experience we had a taxpayer whose net deficiency over the four years examined was less than half the amount of interest assessed on "potential" deficiencies.

Relief for Black Market Operators

The Commissioner of Internal Revenue announced, I. T. 3724, that amounts paid in excess of O. P. A. prices were held not allowable, either as a part of cost of goods sold, or as a business expense deduction in computing Federal income taxes.

But in the case of Lela Sullenger, 11 TC—, No. 127, the Tax Court held that the Commissioner had exceeded his authority, that the 16th amendment permits the taxation of income, not gross receipts, and that income is what remains after cost of goods sold is deducted from sales prices. While this case cannot be relied upon to sustain deductions for above-ceiling prices paid for business expenses, it probably can be used as authority for obtaining allowance for wage and salary payments made in contravention of limitations under the Emergency Price Control Act if such payments were made for direct labor, the cost of which would enter into the cost of goods sold.

More Section 722 Difficulties

Those who are struggling with claims for relief under Section 722 may be interested in, if not encouraged by, this bit of gossip. The Commissioner has recently circulated an unpublished ruling within the Internal Revenue Service, aimed at taxpayers who were found to be guilty of "restraint of trade practices" during the base period. This applies to taxpayers who entered nolo contendere pleas as well as those who were found guilty.

In effect, the Commissioner assumes that the base period earnings of such taxpayers, rather than being abnormally low, were actually higher than they should have been and relief will be denied except in cases where an unusually strong showing is made. This ruling has been applied to all Section 722 claimants who were members of the Southern Pine Lumber Industry and presents an interesting, if superficial, argument in support of the Commissioner's contention that the Southern Pine Lumber Industry was dying, rather than being temporarily depressed, or in the lower segment of a cycle during the base period.

The Commissioner assumes that the Industry's recovery during the base period from the extreme low of the early thirties was the result of illegal trade practices, and that no profits would normally have been earned during the base period except those from illegal practices.

The Commissioner has recently thrown another brick at the Lumber Industry by refusing to allow excess profit credit carrybacks resulting from the application of Section 117 (k). The Bureau contends that Section 117 (k) is a special credit which the statute allows, and that the credit may not be used to reduce the tax of a previous or subsequent year. The Courts will undoubtedly have an opportunity to rule on these questions.

More Reasonable Compensation Cases

When the officers of a corporation own all of its stock, the Bureau is likely to examine salaries paid as to reasonableness. Mentioned by some of the tax services as another taxpayer's victory in reasonable salary cases is that of Grogan Mfg. Co., TC Memo No. 10465, decided in December, 1948, one of our own cases.

The officers of the corporation, and their families, owned practically all of the capital stock. The Commissioner offered evidence that salaries paid officers in the taxable years involved exceeded compensation paid by competitors in those years. The Tax Court held that the fact that the officers had drawn small salaries from 1934 to 1940, and had paid fair dividends, entitled them to substantial increases in the later years, under Lucas v. Ox Fibre Brush Co., 281 U. S. 115.

Along the same line was the case of National Alloys Co., TC Memo No. 14928, where the taxpayer paid no dividends, but the salaries of officers were held to be reasonable in the light of the results produced and the salary rates prevailing in the industry.

Every great advance in science has issued from a new audacity of imagination.

—JOHN DEWEY